Supreme Court, U. S.
FILED
AUG 2 1979
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-1839

ASARCO INCORPORATED (formerly The American Smelting and Refining Company),

Appellant,

v.

IDAHO STATE TAX COMMISSION,

Appellee

ON APPEAL FROM THE
SUPREME COURT OF IDAHO

MOTION TO DISMISS OR AFFIRM

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The Appellee moves the Court to dismiss the appeal herein, or in the alternative, to affirm the judgment of the Idaho Supreme Court on the grounds that the question presented is so unsubstantial as not to need further argument and, alternatively, that the decision of the Idaho Supreme Court is not a final judgment.

I
THE DUE PROCESS ISSUE

Throughout its Jurisdictional Statement Appellant (ASARCO) characterizes its business activities as twofold: (1) Its "operating business" [Jurisdictional Statement, page 7] of mining, smelting, refining and selling ferrous and nonferrous metals, and (2) Its "investment and holding company activities" [J.S., page 10]. The latter is characterized as a separate business having no requisite nexus or situs with the state of Idaho. Therefore, Appellant contends, no part of the income of this allegedly separate business can be apportioned to the state of Idaho. [J.S., page 10-11].

This characterization seriously misconstrues the Idaho Supreme Court's ruling. That Court determined that ASARCO had failed to prove that the dividends, interest and capital gains in question were earned from activities which were separate and distinct from its mining, smelting, refining and selling activities [J.S. App., pages 19, 21 and 22]. It is important to note that where the Idaho court found that ASARCO had established that the activities of dividend-paying subsidiaries were truly "separate and unrelated to ASARCO's general mining and smelting business" the dividends were to be classified as nonbusiness income, none of which could be attributed to Idaho [J.S. App., page 20]. Dividends which the Idaho Court found to result from "more of a separate investment activity than a part of its [ASARCO's] trade or business operations" could not be included in the business income, a part of which would be apportioned to Idaho. [J.S. App., page 20].

But in regard to that income about which ASARCO seeks review, the Idaho Court said:

> The clear inference from these facts is that ASARCO's interest in these companies was not merely that

> of a passive investor but that this dividend income arises from ASARCO's mining and smelting business and that ASARCO acquired and maintained its ownership interest in these companies as an integral and necessary part of its mining and smelting business. [J.S. App. 19]

An accurate understanding of the Idaho Court's decision in this regard is important since the Appellant's Jurisdictional Statement concedes (on pages 10 and 11) that the decisions of this Court allow apportionment of the income of "truly unitary businesses." See *Butler Brothers v. McColgan*, 315 U.S. 501 (1942); *Moorman Mfg. Co. v. Bair*, 437 U.S. 267 (1978); and *Bass, Ratcliff and Gretton v. State Tax Commission*, 266 U.S. 271 (1924). In short, the Idaho Supreme Court has applied the constitutional criteria in precisely the manner the Appellant contends is proper. That is, income which is entirely separate from Appellant's mining, smelting, refining and selling activities may not be attributed to Idaho, even in part, but income earned from the activities which are a part of the unitary business conducted both within and without Idaho may properly be apportioned to Idaho. The only difference of opinion between the Appellant and the Idaho Supreme Court is the Idaho Court's finding that the evidence submitted by ASARCO failed to prove, by clear and convincing evidence, that these particular dividends, capital gains and interest in fact were unrelated to its unitary mining, smelting, refining and selling activities.

The Idaho statute's requirement that a taxpayer prove by clear and convincing evidence that its dividends, interest and gains and losses are not part of its unitary business [*Idaho Code* §63-3027 (a) (1) at J.S. App., page 63] is appropriate since this Court has held that a taxpayer who attacks an apportionment formula carries a distinct burden of showing by "clear and co-

gent evidence" that it results in extraterritorial values being taxed. *Butler Brothers v. McColgan,* supra.

The fact that the Idaho Court did not permit income proven by the taxpayer to be truly separate from its regular trade or business to be apportioned to Idaho clearly distinguishes this case from *Mobil Oil Corp. v. Commissioner of Taxes of Vermont,* U.S. Sup. Crt. Dk. No. 78-1201, jurisdiction noted May 14, 1979. ASARCO's reliance on this Court's noting jurisdiction in *Mobil* is misplaced for two reasons. First, the Uniform Division of Income for Tax Purposes Act (UDITPA) as adopted in Idaho and construed by the Idaho Court clearly limits apportionment solely to the unitary income of a unitary business. Second, in applying the statutory language to the facts as presented by ASARCO, the Idaho court has carefully considered whether the income in question was directly related to the unitary business, a part of which is conducted in Idaho. These factors are entirely absent in the *Mobil* case from Vermont since the Vermont statute requires full apportionment of federal taxable income. The factual issues raised and resolved by the Idaho court were neither raised nor resolved in the Vermont case.

The factual record upon which the Idaho Court based its conclusion is clear. That Court's recital of the facts [J.S. App., pages 4-8] and its holding [J.S. App., pages 16-23] amply reflect the factual basis for concluding that the income challenged by ASARCO is in reality related to its business activities in Idaho. Nor is the Idaho Court alone in this conclusion. The Montana Supreme Court reached the same conclusion in regard to the same taxpayer for the same taxable period. See *Montana Department of Revenue v. American Smelting & Refining Company,* 567 P.2d 901 (Mont., 1977), Appeal Dismissed 434 U.S. 1042 (1978).

As can be seen, therefore, Idaho has apportioned, as a part of ASARCO's unitary business income, earnings accruing to ASARCO as a regular part of its ordinary business activities. It has done so pursuant to a widely adopted uniform statute. This action gives rise to no federal due process questions not resolved by previous decisions of this Court.

The relevant principles are well established. A state may apportion the unitary income of a unitary business by application of the generally recognized three factor formula reflected in the Uniform Act. *General Motors Corporation v. District of Columbia,* 380 U.S. 553 (1965); *Butler Brothers v. McColgan,* 315 U.S. 501 (1942). It is equally well established that an apportionment formula which arrives at a rough approximation of income attributable to a particular state is constitutional. *International Harvester v. Evatt,* 329 U.S. 416, (1947).*

A long and unbroken line of cases upholds the power of states to apportion the unitary income of a unitary business. *Adams Express Company v. Ohio State Auditor,* 165 U.S. 194 (1897), Rehearing 166 U.S. 185 (1897); *Butler Bros. v. McColgan,* 315 U.S. 501 (1942); *Wheeling Steel Corp. v. Fox,* 298 U.S. 193 (1936); *Ford Motor Company v. Beauchamp,* 308 U.S. 331 (1939); *Northwestern Portland Cement Company v. Minnesota,* 358 U.S. 450 (1959); *Complete Auto Transit v. Brady,* 430 U.S. 274 (1977); *Moorman Mfg. Co. v. Bair,* 437 U.S. 267 (1978). This Court has specifically allowed inclusion of the value of intangibles in such an apportionment scheme. See *Adams Express II,* 166 U.S. 185

*For each of the years in question, Idaho seeks the tax of approximately 2.5% of ASARCO's apportionable income based upon the percentage of its total property, payroll and sales attributable to Idaho [Trial Court Stipulation — Clerk's Transcript, pages 40, 44 and 48; Rptr's Trans. 129]. ASARCO seeks to exclude from its apportionable business income the substantial *gross* income amounts shown in Appendix E [J.S. App., page 71]. These amounts represent approximately 70% of its federal net taxable income.

(1897). There is no decision of this Court which requires or even permits the attribution of income from intangibles such as dividends, interest and capital gains to be taxed entirely by the recipient's state of commercial domicile if the income is related to business activities conducted in several states. Instead, cases which recognize the integral role such income, and the subsidiaries generating it, plays in the overall business necessarily suggest a contrary result. See *Flint v. Stone Tracy Co.*, 220 U.S. 107 (1911) and *Ford Motor Company v. Beauchamp*, 308 U.S. 331 (1939). This Court's most recent statement in *Japan Lines v. County of Los Angeles*, 47 USLW 4477 (1979), also tends to a contrary result:

> The correlary of the apportionment principle, of course, is that no jurisdiction may tax the instrumentality in full. "The rule which permits taxation by two or more states on an apportionment basis precludes taxation of all of the property by the state of domicile . . . Otherwise, there would be multiple taxation of interstate operations." *Standard Oil Co. v. Peck*, 342 U.S., at 384-385; *Braniff* [*Airways, Inc. v. Nebraska State Bd. of Equalization*], 347 U.S., at 601. [Bracketed material not in original.]

The due process requirements for apportioning income, as set forth by this Court, are clear and consistent. The Idaho Supreme Court in its opinion below has applied those rules correctly to the factual circumstances which it found before it. Its factual finding, that the income to be apportioned as unitary income, is amply supported by the record. For these reasons, there is no substantial due process federal question presented by this case.

II
THE COMMERCE CLAUSE ISSUE

The test for determining whether a state tax meets the requirements of the Commerce Clause as it applies

to interstate business was established in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), and restated in *Japan Lines Ltd. v. County of Los Angeles*, 47 USLW 4477 (1979). If the state tax "is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State," no impermissible burden on interstate commerce will be found. *Complete Auto Transit, Inc. v. Brady*, supra. In *Japan Lines v. County of Los Angeles*, supra., this Court imposed two additional considerations in the limited case of property taxes directly imposed on "instrumentalities of commerce that are owned, based, and registered abroad and that are used exclusively in international commerce . . ." The two additional considerations required by *Japan Lines* in such circumstances are (1) whether the state tax creates some prohibited risk of double taxation and (2) whether the state tax interferes with federal policy regarding international commerce. Appellant, in its Jurisdictional Statement, relies on *Japan Lines* for the proposition that the Commerce Clause has been violated in this case. This reliance is clearly misplaced.

First, Appellant makes the barefaced allegation in its Jurisdictional Statement (at page 13) that it has experienced double taxation because foreign taxes have been extracted. This is a new contention on the part of Appellant not made at any prior stage in the proceeding. Consequently, the record is entirely devoid of evidence supporting this statement. Regardless of whether it is the actuality or the substantial risk of taxation which is the proper test, it is clear from the decisions of this Court that the taxpayer must prove that the risk or the actuality exist. See *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959); *General Motors Corp. v. Washington*, 377 U.S. 436, 449 (1974); *Standard Pressed Steel Co. v. Department of Revenue of*

Washington, 419 U.S. 560, 563 (1975); *Moorman Mfg. Co. v. Bair,* 437 U.S. 267 (1978).

Furthermore, contrary to Appellant's allegation, including the Appellant's dividends in income subject to apportionment in this case in no way affects foreign commerce. Idaho does not purport nor seek to tax the income of the subsidiaries resulting from their business activities outside the state of Idaho in either interstate or foreign commerce. See Idaho Supreme Court's Decision at J.S. App., pages 24-25. A shareholder is, of course, a taxable entity entirely separate from the corperation issuing the shares. *Moline Properties, Inc. v. Commissioner,* 319 U.S. 436 (1943). The dividend, capital gain and interest income in question represents income earned by ASARCO in the course of its acquisition, management or disposition of certain intangible assets, namely shares of stock in domestically incorporated subsidiaries. For ownership of a domestically incorporated corporation to result in dividends, interest or capital gains payable to its domestic shareholder (whether or not the shareholder happens to be incorporated) is not a transaction occurring in international commerce. Accordingly, the additional requirements imposed by *Japan Lines* do not apply.

The treaties cited by ASARCO do not establish any federal policy which is relevant to this case. These treaties affect only how the United States will tax foreign taxpayers and/or how foreign taxpayers will be taxed in the United States. The treaties establish no policy regarding how domestic taxpayers are to be taxed by the United States or any State.

Finally, even if this Court should find that the inclusion of this income in the income tax base subject to apportionment somehow results in a state tax being directly imposed on international commerce, such a conclusion would neither increase nor decrease the al-

leged risk of multiple international taxation. In *Japan Lines* the finding of multiple taxation lead this Court to conclude that the shipping containers in question were immune from all state property taxation. The Appellant here does not contend that the dividend, interest and capital gains in question are immune from state taxation but only contends that the authority to include it in the tax base is limited to the state of commercial domicile. It is difficult to see how subjecting all of the income to taxation at the state of commercial domicile creates a lesser risk of multiple taxation (on an international level) than does apportioning the same income among several states in which the taxpayer conducts business. To the extent that there is any risk at all, the risk in both circumstances is identical. (We believe, of course, as stated before, that there is no foreign commerce involvement).

The possibility that this income, arising from the domestic transaction of receiving dividends, interest or capital gains from a domestic subsidiary, may be subject to some overlap of state taxation does not, by itself, render the Idaho tax invalid. This Court said in *Moorman Mfg. Co. v. Bair,* supra., at 272-273:

> . . . Yet even were we to assume that the Illinois activities made some contribution to the profitability of the Iowa sales, appellant's claim that the Constitution invalidates an apportionment formula whenever it may result in taxation of some income that did not have its source in the taxing State is incorrect.
>
> The Due Process Clause places two restrictions on a State's power to tax income generated by the activities of an interstate business. First, no tax may be imposed unless there is some minimal connection between those activities and the taxing state. [Citation omitted] This requirement was plainly satisfied here. Second, the income attributed to the State for

tax purposes must be rationally related to "values connected with the taxing state." [Citation omitted]

Since 1934, Iowa has used the formula method of computing taxable income. This method, unlike separate accounting, does not purport to identify the precise and geographical course of a corporation's profits; rather, it is employed as a rough approximation of a corporation's income that is reasonably related to the activity conducted within the taxing State. The single-factor formula used by Iowa, therefore, generally will not produce a figure that represents the actual profits earned within the State. But the same is true of the Illinois three-factor formula. Both will occasionally over-reflect or under-reflect income attributable to the taxing State. Yet despite this imprecision, the Court has refused to impose strict constitutional restraints on a state's selection of a particular formula.

In summary, it is clear that the Idaho tax meets the fourfold test of *Complete Auto Transit v. Brady,* supra. The additional requirements imposed by *Japan Lines,* supra., are, at their greatest extent, limited to transactions or instrumentalities occurring in foreign commerce which create a demonstrated risk of multiple taxation on an international basis. Those criteria simply do not apply to the circumstances presented by this case.

III
THE DECISION OF THE IDAHO SUPREME COURT IS NOT A FINAL JUDGMENT

The jurisdiction of this Court to review the decision of the Idaho Supreme Court is, of course, based upon 28 U.S.C., §1257 which limits the appellate jurisdiction of this Court to review of "final judgments." The Idaho Supreme Court's decision (J.S. App., pgs. 30-32) remanded the case to the trial court for a determination of

certain factual issues relating to the proper determination of the sales factor portion of the apportionment formula. The Appellant contends (J.S. page 3) that this issue is purely one of statutory interpretation and is entirely separate from the constitutional questions upon which the Appellant seeks review. The Appellant cites *Cox Broadcasting Corp. v. Cohn,* 420 U.S. 469 (1975); and *Radio Station WOW v. Johnson,* 326 U.S. 120 (1945), which support the general proposition that under certain circumstances, established by those cases, the Court may indeed assume appellate jurisdiction even though further proceedings in the case on the state court level are contemplated. The difficulty with the Appellant's contention is that the issue remanded by the Idaho court to the trial court is not severable from the issues upon which the Appellant seeks review but is necessarily related. A determination of the proper application of the sales factor under the UDITPA three-factor formula is necessary before it can be finally known what absolute amount or portion of ASARCO's total income Idaho will deem to have been earned from Idaho sources. This Court has held that a state taxing scheme must be judged based upon the result which it reaches. For example, in *Hans Rees' Sons v. N. Carolina,* 283 U.S. 123 at 135 (1931), the court held a North Carolina tax unconstitutional because "... [T]he statutory method, as applied to appellant's business for the years in question operated unreasonably and arbitrarily, in attributing to North Carolina a percentage of income all out of appropriate proportion to the business transaction transacted by the appellant in that State."

Other decisions also support the proposition that a state tax must be measured based upon its known result. In *Wisconsin v. J.C. Penny Company,* 311 U.S. 435, 444 (1940), the Court stated:

> That test is . . . whether the taxing power exerted by the state bears fiscal relationship to protection, op-

portunities and benefits given by the state. The simple but controlling question is whether the state has given anything for which it can ask return.

See also *Hump Hairpin Co. v. Emmerson,* 258 U.S. 290, 296 (1922) and *International Harvester v. Evatt,* 329 U.S. 416 (1947).

So long as the state courts have yet to determine how the sales factor portion of the three-factor UDITPA formula is to be applied to this taxpayer, the full extent of this taxpayer's income which the state is subjecting to income taxes is not known.

It is important that the entire apportionment formula as used in UDITPA and enacted in Idaho be clearly understood. It is found in *Idaho Code* §63-3027. (J.S. App., page 63) The steps for determining the amount of an interstate taxpayer's income which is attributable to Idaho are as follows: First, the total net taxable income from all activity and sources both within and without the state of Idaho is determined. Second, the amount of nonbusiness (nonunitary) income is computed and subtracted from the amount determined in step one. This result is the net business (unitary) income subject to apportionment. Third, an apportionment factor is computed. This apportionment factor is the average of three factors — sales in the taxing state divided by sales everywhere plus real and tangible personal property in the taxing state divided by such property everywhere plus payroll in the taxing state divided by payroll everywhere. Fourth, the apportionment factor as computed in the third step is applied to the net apportionable business income computed in the second step to determine the amount of apportionable income to be attributed to the taxing state. Fifth, any nonbusiness income found to be allocable in its entirety to the taxing state is added to the result determined in the fourth step. This sum represents the income subject to the tax

in the taxing state and to which that taxing state's tax rate may be applied.

The record does not reflect the precise amount of ASARCO's taxable income attributed to Idaho which a resolution of the sales factor issue might affect. The record does reflect that virtually all of the sales attributed to Idaho are included in the disputed amount. It is reasonable to conclude, therefore, that approximately one-third of ASARCO's total income tax liability to the state of Idaho remains in question.

Therefore, it can be clearly seen that the issues decided by the Idaho Supreme Court and the issue remanded by it to the trial court for further decision are inextricably tied together since all of the issues relate to the determination of variables in the same apportionment formula. The constitutional test by which that formula is measured is whether or not it attributes an amount of income which is in "appropriate proportion to the business transacted by the appellant" in the state of Idaho. [*Hans Rees' Sons,* supra.] Interestingly, Appellant's Jurisdictional Statement (on page 11) appears to agree that it is the *result* of the apportionment process by which the constitutional validity of that process must be measured.

CONCLUSION

For the reasons stated herein, this appeal should either be dismissed or affirmed.

DATED THIS 31st day of July, 1979.

Respectfully submitted,

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